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No. 152

Supreme Court of the United States.

OCTOBER TERM, 1942.

EVERIT B. TERHUNE ET AL., EXECUTORS UNDER THE WILL OF WILLIAM L. TERHUNE,
Petitioners,

v.

WILLIAM M. WELCH, COLLECTOR.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

AND

BRIEF IN SUPPORT THEREOF.

CLEMENT R. LAMSON,
RALPH C. PIPER,
Attorneys for the Petitioner.

ADDISON C. GUTCHELL & SON, LAW PRINTERS, BOSTON.

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v.
WILLIAM M. WELCH, COLLECTOR.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The undersigned, on behalf of Everit B. Terhune *et al.*, executors under the will of William L. Terhune, pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the First Circuit, rendered on March 23, 1942, in the case of William M. Welch, Collector (Defendant, Appellant), *v.* Everit B. Terhune *et al.*, Executors (Plaintiffs, Appellees).

Opinions Below.

The opinion of the Circuit Court of Appeals is reported in 126 Fed. (2d) 695. The opinion of the District Court of the United States for the District of Massachusetts is reported in 39 Fed. Supp. 430.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on March 23, 1942 (R. 56). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925. The action to which this petition relates is an action against the Collector of Internal Revenue to recover a tax unlawfully assessed and collected.

Question Presented.

The question stated generally is whether, under Section 302 (d) of the Revenue Act of 1926 as it stood before its amendment by Section 805 of the Revenue Act of 1936, the corpus of a trust established during his lifetime in 1929 by the plaintiffs' testator, William L. Terhune, is properly included as part of the gross estate of the decedent to measure an estate tax by reason of the existence of a clause in the instrument creating the said trust under which the trust might be terminated or amended by the trustees (of whom the settlor was one) and beneficiaries entitled after the decedent's death to all of the income if they survived him and to approximately five-sixths of the principal if they survived him for ten years.

Statement of the Case.

In 1929 the decedent, William L. Terhune, a widower seventy-nine years old, was about to contract a second marriage with a woman who was younger than his three children born of his first marriage (R. 37). For the purpose of so arranging his affairs that no friction would develop between his children and the second wife (see the opinions

of the District Court (R. 37) and of the Circuit Court of Appeals (R. 48)), he transferred the principal portion of his estate (R. 38) to a trust, of which the settlor, William L. Terhune, his son and a son-in-law were the trustees, and the latter two persons were the trustees after his decease. The income was to be paid to the decedent for life. Provision was made for the second wife, but was conditioned on her being the decedent's widow (R. 14, 17), and therefore became void in 1931, since she was divorced from the decedent in that year (R. 36), whereupon he married for the third time (R. 37). After the decedent's death, income was to go to his three children for ten years, when they were to receive all the principal except $70,000 (R. 15). His children's issue were to take parent's share if any of them should die before the principal became distributable.

Clause 12 of the trust instrument read as follows (R. 21): "This Trust may be terminated or amended at any time, but only with the written consent of the three Trustees herein named, and of any Trustee appointed by William L. Terhune under clause 14 hereof, or the survivors or survivor of them, and of the then surviving children of the said William L. Terhune." Clause 14 (R. 22) gave the decedent the right "to appoint another co-trustee to act with the three herein named, . . ." No such co-trustee was ever appointed.

The decedent died on February 23, 1936. His three children survived him. The corpus of the trust at the time of the decedent's death was valued at $394,506.27 (R. 35), and his own estate was valued at about $40,000 (R. 34). The Commissioner of Internal Revenue, relying on Section 302 (c) and 302 (d) of the Revenue Act of 1926, required the inclusion of the full value of all interests in the trust property in the decedent's gross estate (R. 25-28). The executors paid a deficiency tax of $56,542.53 with interest (R. 35) and brought suit for its recovery against the Collector

of Internal Revenue in the District Court. The District Court gave judgment for the taxpayer, holding that neither ground asserted by the Commissioner warranted the tax (R. 43). The Collector appealed (R. 44). In his argument on appeal, the Collector relied on Section 302 (d) and on that part of Section 302 (c) dealing with transfers intended to take effect in possession or enjoyment at or after death (R. 56).

The Circuit Court of Appeals reversed the judgment in favor of the taxpayer on the ground that Section 302 (d) applied, but did not expressly pass on the point raised under Section 302 (c) (R. 56).

Statutes Involved.

The statutes involved are Section 302 of the Revenue Act of 1926 (as it stood before its enactment by Section 805 of the Revenue Act of 1936) and its sub-section (d) (c. 27, 44 Stat. 9, 70, 71). The material portions read as follows:

> "Sec. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated— . . .
>
> "(d) To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth. . . ."

Specifications of Errors to be Urged.

The petitioners submit that the Circuit Court of Appeals erred—

(1) in failing to follow the reasoning in *Helvering* v. *City Bank Farmers Trust Co., Trustee,* 296 U.S. 85, by failing to hold in accordance therewith that Congress had not created by Section 302 (d) a fictitious status by which the property transferred by trust in the instant case was rendered includable for estate tax purposes as part of the estate of the deceased settlor;

(2) in failing to follow the case of *Helvering* v. *Helmholz,* 296 U.S. 93, by failing to hold in accordance therewith that no interest in the property transferred by trust in the instant case was rendered includable for estate tax purposes as part of the estate of the deceased settlor by Section 302 (d);

(3) (alternative to or in addition to points (1) and (2)), in failing to hold that the interest of none of the three children of the deceased in the trust property was rendered includable for estate tax purposes as part of the estate of the deceased settlor by Section 302 (d);

(4) by failing to hold that, since any power in the settlor to change enjoyment was lodged in him only in his capacity as trustee, Section 302 (d) did not render the trust property includable for estate tax purposes as part of the estate of the deceased settlor (*Nicholson* v. *United States,* 25 Fed. Supp. 424, and decision of District Court in instant case);

(5) in holding Section 302 (d) of the Revenue Act of 1926 applicable to the trusts in question;

(6) in reversing the judgment of the District Court.

Reasons Why the Writ should be Granted.

1. The Circuit Court of Appeals has in this case decided a federal question in a way probably in conflict with appli-

cable decisions of this Court in holding that Congress has, by Section 302 (d) of the Revenue Act of 1926, through setting up a presumption or a "fictitious status under the guise of supposed necessity" (City Bank case, p. 92), provided that the property here settled in trust can be regarded as part of the estate of the deceased settlor so that such property can be used to measure the estate tax, in direct contradiction to the combination of actualities in this case, as follows:

(*a*) No change in enjoyment of the trust property could have been made without the consent of the three owners of practically the entire beneficial interests in the property; plus the assent of a fourth person, a trustee.

(*b*) The deceased could have participated in any change in the enjoyment of the trust property only in a fiduciary capacity, as one of three trustees under a duty to act with the utmost good faith and only in the interest of all the beneficiaries.

(*c*) The two trustees other than the deceased whose consent to any change of enjoyment was necessary would have had to participate therein in a fiduciary capacity as trustees of the property under a duty to act with the utmost good faith and only in the interest of all the beneficiaries.

(*d*) The value of the settlor's property at the date of his death was approximately one-tenth of the value of the corpus of the trust.

(*e*) The purpose of the trust has been found by the District Court and repeated by the Circuit Court to have been to avoid certain anticipated friction, and therefore not to evade or even to avoid estate taxes.

2. The Circuit Court of Appeals has decided erroneously an important question of federal law considered in the case of *Helvering* v. *Helmholz* and the case of *Helvering* v. *City Bank Farmers Trust Co.* relating to the nature, the scope

and extent of the power to change the enjoyment of property transferred by trust by a decedent which will cause the value of such property under the provisions of Section 302 (d) of the Revenue Act of 1926 to be used to measure a tax on the estate of a decedent, which question should be settled by this Court

(*a*) to clear up the uncertainty and confusion directly relating to a correct decision of the instant case now existing in the minds of courts and commentators and of others as to the scope and effect of the decisions of this Court in said Helmholz and City Bank cases; and

(*b*) to prick out a line in connection with the reasoning in the City Bank case indicating cases which are and cases which are not within the power of Congress to establish a conclusive presumption that property settled by a decedent in trust during his lifetime is part of his estate on his decease for measuring the estate tax on account of a power to change enjoyment, which line "cannot be drawn by generalities but successive points must be fixed by weighing the particular facts." See opinion of Mr. Justice Holmes in the case of *Frost Trucking Co.* v. *Railroad Commission,* 271 U.S. 583, 601.

Some of these conflicting interpretations can be found in *Commissioner* v. *Allen,* 108 Fed. (2d) 961, 965 (Helmholz case interpreted as turning on the power coming to the settlor as one of the beneficiaries and not as the settlor).

Howard v. *United States,* 125 Fed. (2d) 986 (Helmholz case interpreted as turning on the trust indenture becoming terminable by the joint act of all the beneficiaries).

55 Harvard Law Review, 684 (Helmholz case interpreted as based on power to change enjoyment being in "the then living beneficiaries," *i.e.,* beneficiaries living at the date of the death of the settlor).

Section 302 (d) has been in effect, from 1924 to 1936, unmodified so far as the present questions are concerned.

During that period it is to be inferred that numerous trusts have been created with various reserve powers to change enjoyment, the effect of which powers, with respect to Section 302 (d), will not come before the courts until the various settlors shall have deceased.

BRIEF.

Section 302 imposes an estate tax—an excise tax based on the value of property passing from the dead to the living—not a delayed tax on gifts which were completed during the lifetime of the deceased. *Heiner* v. *Donnan*, 285 U.S. 312, 322; *Reinecke* v. *Northern Trust Co.*, 278 U.S. 339.

Section 302 (d) creates a presumption that in certain cases property, legal title to which is not in the estate of a decedent at his death, having been transferred by him during his lifetime, shall nevertheless be regarded as part of his estate for measuring the estate tax. The purpose of Section 302 (d) is to prevent the evasion of tax (City Bank case, p. 91) through transfers in cases where the transferors retain substantial control over the economic interests of the property transferred. That "substantial control" over the property by the settlor is necessary for the creation of the presumption provided for by Section 302 (d) is indicated by the following paragraph from the Report of the Chairman of the House Ways and Means Committee (House Report 179, 68th Congress, First Session, p. 28), referring to said Section 302 (d):

> "Even though the decedent has made the transfers specified in this subdivision, he has retained substantial control over the disposition of the property, through the power to change the enjoyment thereof. Such prop-

> erty interests should therefore fairly be taxed as part of the decedent's estate, particularly since, by virtue of his death, the substantial interest which he had has been wiped out, and to the same extent the property interest of the legal title holder, his transferee, has been increased. This provision is in accord with the principle of section 219(g) of the bill which taxes to the grantor the income of a revocable trust."

It is to be inferred from the above that, where the power of the decedent at the time of his death to change the enjoyment of a property interest in a trust he had created did not constitute "substantial control over the disposition of the property," Section 302 (d) was not intended to apply. Also the City Bank case declares that "there are, however, limits to the power of Congress to create a fictitious status under the guise of supposed necessity."

The facts in the City Bank case showed a transfer in trust clearly within the scope of the presumption, since the settlor in that case retained substantial control over the economic interests in the property after its transfer in trust, as she could change the enjoyment of the trust property with the assent of only one beneficiary, her husband, whose interest was contingent and small in value with reference to all the other interests in the trust. *The instant case is nearly at the opposite pole from the City Bank case and is as if in the City Bank case all the interests whose assents were not there necessary had, in fact, been necessary.*

Even though by its terms said Section 302 (d) did require that the trust property in this case be included as a measure of an estate tax, it should nevertheless be excluded since to include it would cast doubts, to say the least, on the constitutionality of the statute. The statute should not be construed literally, if to do so would give it an unreasonable or unconstitutional application. *Holy Trinity Church* v.

United States, 143 U.S. 457. "A statute must be construed, if fairly possible, so as to avoid not only the conclusion that it is unconstitutional but also grave doubts upon that score." *United States* v. *Jin Fuey Moy*, 241 U.S. 394, 401.

Even if it be admitted that Section 302 (d) might be properly applicable in some cases where tax avoidance was found expressly not to have been the purpose of the transfers in trust, nevertheless it is urged that in conjunction with all the other facts indicating the tenuity of any power in the settlor in this case to change enjoyment, it is important here that the purpose of the trust has been found to have been to avoid friction between the decedent's second wife and his children by his first marriage, and therefore, not to avoid or to evade estate taxes.

Moreover, it would have been impossible for the settlor in this case to have bought off his children, since his own property was much less in the aggregate than the value of any one of his children's interest in the trust estate.

The attenuated nature of the decedent's power to change enjoyment is emphasized if one considers the interests of the three children in the trust property in connection with any such power. In order to change the enjoyment of any one of his three children, the settlor would have had to persuade not only such child but two other children having similar interests and (one of such children being a trustee) another person, also a trustee, but having no beneficial interest in the trust property. For a case where interests in trust property have been treated separately with reference to the application of Section 302 (d) see the case of *Commissioner of Internal Revenue* v. *Bridgeport City Trust Co.*, 124 Fed. (2d) 48. A gift can hardly be regarded as having "strings attached" where the only chance of the donor of recovering back the gift is to persuade the donee to give it back, and where there is no pecuniary inducement to make such gift back and where, as in this case, not only

each child would have had to be persuaded but the other persons as stated above.

Quite apart from the fact that there could be no change in enjoyment without the consent of the owners of practically all the beneficial interests of the trust, it is to be noted that the clause with reference to termination or amendment (clause 12 of the trust instrument (R. 21)) did not give the settlor any power whatever as settlor, and there is no intimation that the settlor was even to initiate any proceedings to terminate or amend. In the case of *Reinecke* v. *Smith*, 289 U.S. 172, and *Chickering* v. *Commissioner*, 118 Fed. (2d) 254, the deceased had virtually a power in gross in that he could have participated in the exercise of any power to change enjoyment even after he had ceased to be a trustee. In the cases of *Witherbee* v. *Commissioner*, 70 Fed. (2d) 696, and *Carkhuff* v. *Commissioner*, 83 Fed. (2d) 626, the deceased, by the terms of the trust, reserved the power to himself to change enjoyment and was not a trustee. Had the deceased in the instant case as trustee, the only capacity in which he had any authority whatever to participate in any change of enjoyment, undertaken to disregard the interests of the beneficiaries of the trust, he would have been violating the rule that no trustee can act in his own interest in conflict with that of the beneficiaries. See Restatement of the Law of Trusts, Section 187 d(6). There is nothing to intimate that the trustees other than the decedent were in any way his agents. "When there are two or more beneficiaries of a trust, the trustee is under a duty to deal impartially with them" (Restatement of the Law of Trusts, Section 183), and each trustee must use reasonable care to prevent a co-trustee from committing a breach of trust (Restatement of the Law of Trusts, Section 184). "The trustee is under a duty to the beneficiary to administer the trust solely in the interest of the beneficiary" (Restatement of the Law of Trusts, Section

170). In this case, therefore, any power to change enjoyment residing in the decedent at the time of his death was held by him in a fiduciary capacity, as one of the three trustees of the trust. Had the trust property remained his own, he could have dealt with it in all respects as he liked, but as a trustee any power he had over it must be exercised with the utmost regard for the rights of the beneficiaries, and his power to handle the property on an arm's length basis became non-existent when he created the trust. Had he been disposed in any way to treat the trust property as his own in violation of his duty as a trustee, there were two other trustees and the Massachusetts courts to see that he did not do so, and in addition there were all three of his children together holding practically the entire beneficial interests in the trust, as well as certain grandchildren holding smaller interests therein (see *Nicholson* v. *United States,* 25 Fed. Supp. 424).

Even if Section 302 (d) of the Revenue Act of 1926, applicable in this case, had contained the amendment thereto, namely, the words "in whatever capacity acting," added by the Revenue Act of 1936 (Section 805, Revenue Act of 1936, 49 Stat. 1744-45), or had such amendment had the rather retroactive effect given it by the Circuit Court in this case (R. 55), it is obvious, of course, that the contention of these petitioners herein contained would have been no different, to the effect that no intention can be imputed to Congress to include the corpus of an *inter vivos* trust to measure the estate tax of a settlor unless at the time of his death he had substantial control over it.

Boyden v. *Stevens,* 285 Mass. 176, at 179: "There is an implication, when even broad powers are conferred, that they are to be exercised with that soundness of judgment which follows from a due appreciation of trust responsibility. Prudence and reasonableness, not caprice or careless good nature, much less a desire on the part of the trustee

to be relieved from trouble or from the possibility of making a foolish investment, furnish the standard of conduct." *Corkery* v. *Dorsey,* 223 Mass. 97, 101. See also *Wilson* v. *Wilson,* 145 Mass. 490, 492.

Although it may be unnecessary for these petitioners to refer to the case of *Helvering* v. *Helmholz* as an authority to sustain their contentions herein made, it is nevertheless contended that that case is on all fours with the instant case and, if followed, will result in a reversal of the decision of the Circuit Court of Appeals. In that case the essential facts were that the decedent had transferred certain property in trust, the income to be paid to her for life, and after her death to be paid for life to her appointees by will, and in default of appointment, or after the appointees' death, to her issue, and in default of issue, to other relatives or their issue, and upon termination of the trust the principal was to be paid to the persons then entitled to the income. The trust was to terminate on the death of certain named persons or among other contingencies "upon delivery to the said trustee of a written instrument signed by all of the then beneficiaries . . . declaring said trust term at an end," the quoted words contained in the trust instrument being those relied upon to render the trust fund includable for estate tax purposes. The words "then beneficiaries" have been interpreted in a learned note in the Harvard Law Review (55 Harvard Law Review, 684) as meaning then living beneficiaries, that is, beneficiaries living at the date of the death of the settlor. This interpretation, it is submitted, is the correct one, for had the assent of all the beneficiaries been necessary there would have been no power at all, since many beneficiaries were unborn and unascertained persons, whose assents could not have been obtained at any time prior to the termination of the trust by its express terms. On the basis of this interpretation, the case is on all fours with the instant case in that (*a*)

Section 302 (d) was in effect in identical form in both the Helmholz case and in this case; (*b*) the law of Wisconsin, as it was presumed to exist by this Court in the Helmholz case, was the same as the Massachusetts law applicable to this case, namely, as set forth in Section 338 of the Restatement of the Law of Trusts, "§ 338. This states the law"—see Massachusetts Annotations to the Restatement of the Law of Trusts, Section 338, p. 282; (*c*) the interests of the beneficiaries living at the death of the settlor in the Helmholz case corresponded in the proportion they bore in terms of value to all the interests created by the trust instrument in the trust property to the proportion borne by the interests whose assents would be required to any change in interest bore to all the interests in this case. The Helmholz case was, it is submitted, like this case, one which, were Section 302 (d) to be held applicable thereto, would have been beyond the "limits to the power of Congress to create a fictitious status under the guise of supposed necessity" (City Bank case, p. 92). Moreover, in the instant case, as is pointed out at more length hereinbefore, any power in the settlor to change any interest in the trust could be exercised by him only as trustee, which was not true in the Helmholz case.

It may well be that the Court in the Helmholz case was of the opinion that had Section 302 (d) been held applicable "the individual innocent of evasion" would have been "stripped of his constitutional rights in order to further a more thorough enforcement of the tax against the guilty —a new and startling doctrine condemned by its mere statement and distinctly repudiated by this Court in the Schlesinger (240) and Hoeper (217) cases, involving similar situations." *Heiner* v. *Donnan,* 285 U.S. 312, at 328.

In *Haddock* v. *Haddock,* 201 U.S. 562, 631, Holmes, dissenting, said: "I have heard it suggested that the difference is one of degree. I am the last man in the world to quarrel

with a distinction simply because it is one of degree. Most distinctions, in my opinion, are of that sort, and are none the worse for it. But the line which is drawn must be justified by the fact that it is a little nearer than the nearest opposing case to one pole of an admitted antithesis.

Conclusion of Brief.

No case has been found in which this Court or any other court has held the conditions of Section 302 (d) to be satisfied where the deceased could participate in the change in enjoyment of the trust property only in a fiduciary capacity as is the case here. No case has been found where such conditions have been held to be satisfied where the participation of the deceased in any change of enjoyment has been so circumscribed and attenuated as in this case, requiring for any change of enjoyment the concurrence of three trustees and of the three beneficiaries owning very nearly the entire sum of the beneficial interests in the trust property. Any substantial change in enjoyment in this case would necessarily have involved a substantial change in the beneficial interests of such three beneficiaries and their consent would have been necessary. It is submitted that it is beyond all reason to presume that any such consent could have been obtained. Surely Congress can enact reasonable provisions to prevent the evasion of estate taxes and to that end can create reasonable presumptions. But the presumption held by the court below to have been created by Section 302 (d) in this case is, it is submitted, far outside of any rule of reason, applicable to the prevention of tax avoidance. "Rights guaranteed by the federal Constitution are not to be so lightly treated; they are superior to this supposed necessity. The State is forbidden to deny due process of law or the equal protection of the

laws for any purpose whatsoever." *Heiner* v. *Donnan*, 285 U.S. 312, 325.

A writ of certiorari in this case will, in addition to its bearing hereon, result, it is reasonably to be expected, in establishing or tending to establish the principle on the basis of which many future cases, which it is to be expected will arise hereafter, may be decided. "Tax laws like all other laws are made to be obeyed. They should therefore be intelligible to those who are expected to obey them." *Philadelphia Storage Battery* v. *Lederer*, 21 Fed. (2d) 320, 321, 322, and *White* v. *Aronson*, 302 U.S. 16, at 20. "Numerous cases pending in the courts and the Board of Tax Appeals involving these questions, and the claim that decisions of this Court have not settled the matter, moved us to grant certiorari." Per Roberts, J., in *Hassett* v. *Welch*, 303 U.S. 303, 305.

CONCLUSION.

Wherefore it is respectfully submitted that this petition for a writ of certiorari should be granted.

CLEMENT R. LAMSON,
RALPH C. PIPER,
Attorneys for the Petitioners.

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v.

WILLIAM M. WELCH, COLLECTOR

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The opinion of the District Court (R. 37–43) is reported in 39 F. Supp. 430. The opinion of the Circuit Court of Appeals (R. 47–55) is reported in 126 F. (2d) 695.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 23, 1942. (R. 55–56.) The petition for a writ of certiorari was filed on June 16, 1942. The jurisdiction of this Court is predi-

cated upon Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The decedent created a trust in 1929, reserving the income to himself for life, and naming himself as one of the trustees. He also reserved the power to terminate or amend the trust in conjunction with the other trustees and some of the beneficiaries. Is the corpus of the trust includible in his gross estate under Section 302 (d) of the Revenue Act of 1926?

STATUTES AND OTHER MATERIAL INVOLVED

The statutes, regulations, and committee report involved appear in the Appendix, *infra*, pp. 7–13.

STATEMENT

This is an action for the recovery of an alleged overpayment of estate tax upon the estate of William L. Terhune, who died on February 23, 1936. The alleged overpayment was made pursuant to a determination by the Commissioner of Internal Revenue that the assets of a trust created by the decedent on May 6, 1929, were includible in his gross estate (R. 1–23, 25–28).

The trust, which is evidenced by two indentures executed simultaneously on May 6, 1929 (R. 5, 13), was created by the decedent at a time when he was 79 years of age. Its corpus consisted of the principal portion of his property and it was

created in order to avoid possible friction between his children and a second wife whom he was then about to marry. The named trustees were the grantor, his son, and his son-in-law (R. 37, 38).

The net income of the trust was payable to the decedent during his life; after his death, the income and corpus were to be distributed among his descendants and his second wife in accordance with provisions which are set forth in detail in the trust instruments, but do not appear to be material here (R. 14–17).

The indentures provided that during his lifetime the decedent should be the active trustee with complete power to manage the trust by himself (R. 8, 20). It was also provided that he could delegate his active authority to any of the other trustees (R. 9, 21), and that he could appoint a fourth trustee at any time after June 10, 1929 (R. 11, 22). Both indentures contained the following critical provision (R. 10, 21):

> 12. This Trust may be terminated or amended at any time, but only with the written consent of the three Trustees herein named, and of any Trustee appointed by William L. Terhune under clause 14 hereof, or the survivors or survivor of them, and of the then surviving children of the said William L. Terhune.

The Commissioner ruled that the corpus of the trust was includible in the decedent's gross estate and determined a deficiency accordingly (R. 25–

28). The decedent's executors paid the deficiency and then brought this suit for refund. The District Court held that the corpus of the trust was not includible in the decedent's gross estate and entered judgment for the plaintiffs in the amount of $57,669.53 plus interest thereon (R. 36). The Circuit Court of Appeals reversed, holding that Section 302 (d) of the Revenue Act of 1926 required the trust to be included in the gross estate (R. 55–56).

ARGUMENT

The decision below is correct. There is neither a conflict, nor any other reason warranting further review.

Section 302 (d) of the Revenue Act of 1926, c. 27, 44 Stat. 9 (Appendix, *infra,* p. 7), requires the inclusion in a decedent's gross estate of the corpus of a trust created by him if the enjoyment thereof "* * * was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, * * *."[1] Since the grantor in this case named himself one of the trustees, he had reserved the right under paragraph 12, quoted above, to terminate *or amend* the trust in conjunction with the

[1] At the time of the decedent's death, February 23, 1936, this section had been amended by Section 401 of the Revenue Act of 1934, c. 277, 48 Stat. 680, Appendix, *infra*, p. 7, but not in any respect here material.

others mentioned therein. The corpus must therefore be included in his gross estate, notwithstanding that the other persons were beneficiaries or had an interest in the trust. *Helvering* v. *City Bank Co.*, 296 U. S. 85. There is no foundation for petitioners' contention that the powers to terminate or amend were of a fiduciary nature and therefore not within the statute. Cf. *Reinecke* v. *Smith*, 289 U. S. 172, 176–177.

There is no conflict with *Helvering* v. *Helmholz*, 296 U. S. 93, in which the Court held the predecessor provisions of Section 302 (d) in the Revenue Act of 1924 unconstitutional as applied to a trust created prior to their enactment. On the same day, the Court held those provisions valid in the *City Bank* case, *supra*, as applied to a trust established after they became law. And as in the *City Bank* case, the trust herein was created after the enactment of the critical provisions of the revenue act.

It is of no significance that the grantor's powers to terminate or amend were reserved to him "as trustee" rather than "as grantor." The statute draws no such fine distinction, and a clarifying amendment made by Section 805 of the Revenue Act of 1936 (Appendix, *infra*, p. 9) makes clear that the power is within the statute "in whatever capacity exercisable." [2]

[2] The amendment was occasioned by *White* v. *Poor*, 296 U. S. 98, in which the existing provisions were held inapplicable to a case where the grantor's power relied upon by the

CONCLUSION

There is no conflict with any decision of this Court or any other court. The decision below is correct. The petition should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
BERNARD CHERTCOFF,
Special Assistants to the Attorney General.

JULY 1942.

Government had not been reserved but had been bestowed upon her after the trust had been created. To the extent that the 1936 amendment deals with powers *retained* by the grantor in whatever capacity exercisable, it is merely declaratory of existing law. See Article 20, Treasury Regulations 80 (1937 Ed.); cf. H. Rep. No. 2818, 74th Cong., 2d Sess., pp. 9–10 (Appendix, *infra*, pp. 11–13).

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated—
>
> * * * * *
>
> (d) To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth. * * *
>
> * * * * *

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 401. REVOCABLE TRUSTS.
>
> Section 302 (d) of the Revenue Act of 1926 is amended to read as follows:
>
> "(d) (1) To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, or where the

decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth.

"(2) For the purposes of this subdivision the power to alter, amend, or revoke shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the alteration, amendment, or revocation takes effect only on the expiration of a stated period after the exercise of the power, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised. In such cases proper adjustment shall be made representing the interests which would have been excluded from the power if the decedent had lived, and for such purpose if the notice has not been given or the power has not been exercised on or before the date of his death, such notice shall be considered to have been given, or the power exercised, on the date of his death.

"(3) The relinquishment of any such power, not admitted or shown to have been in contemplation of the decedent's death, made within two years prior to his death without such a consideration and affecting the interest or interests (whether arising from one or more transfers or the creation of one or more trusts) of any one beneficiary of a value or aggregate value, at the time of such death, in excess of $5,000, then, to the extent of such excess, such relinquishment or relinquishments shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this title;"

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 805. ESTATE TAXES—REVOCABLE TRANSFERS.
>
> (a) Section 302 (d) (1) of the Revenue Act of 1926, as amended, is amended to read as follows:
>
> "(d) (1) To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona-fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished in contemplation of decedent's death."
>
> (b) Except in the case of transfers made after the date of the enactment of this Act, no interest of the decedent of which he has made a transfer shall be included in the gross estate under such section 302 (d) (1) unless it was includible under such section before its amendment by this section.

Regulations 80 (1937 Ed.):

> ART. 20. *Transfers with power to change the enjoyment.*—(a) *Transfers included.*—Subdivision (d) of section 302 of the Revenue Act of 1926, as amended, embraces a transfer by trust or otherwise (if not amounting to a bona fide sale for an adequate and full consideration in money or money's worth) when at the time of dece-

dent's death the enjoyment of the transferred property, or some part thereof or interest therein, was subject to any change through a power exercisable either by the decedent alone, or by him in conjunction with some other person or persons, to alter, or amend, or revoke, or terminate. (See article 15.)

The addition to the subdivision, by section 805 of the Revenue Act of 1936, of the phrase to the effect that it is not material in what capacity the power was subject to exercise by the decedent or by the other person or persons in conjunction with the decedent, is considered as merely declaratory of the meaning of the subdivision prior to the addition of the phrase.

The second phrase added by amendment in 1936 (namely, "without regard to when or from what source the decedent acquired such power") is not considered declaratory of the meaning of the subdivision prior to the amendment in a case in which no one of the powers enumerated in the subdivision was reserved at the time of the making of the transfer, but one or more thereof was conferred subsequent thereto (whatever the source from which conferred) without any understanding, expressed or implied, had in connection with the making of the transfer that such power or powers should be later conferred.

The third change made in the subdivision by the Revenue Act of 1936 consisted of the addition of the words "or terminate" following the words "to alter, amend, revoke." Such addition is considered but declaratory of the meaning of the subdivision prior to the amendment. A power to terminate capable of being so exercised as to revest

in the decedent the ownership of the transferred property or an interest therein, or as otherwise to inure to his benefit or the benefit of his estate, is, to that extent, the equivalent of a power to "revoke," and when otherwise so exercisable as to effect a change in the enjoyment, is the equivalent of a power to "alter."

* * * * *

H. Rep. No. 2818, 74th Cong., 2d Sess., pp. 9–10:

Section 206 amends section 302 (d) (1) of the Revenue Act of 1926, as amended, relating to the inclusion in the gross estate of a decedent of the value of property, transferred by him by trust or otherwise, but subject to a power to alter, amend, or revoke. The changes made by this section are made necessary largely by reason of the decision of the United States Supreme Court in the case of *White* v. *Poor* (296 U. S. 98). Although in that case the decedent had created a trust which was at her death subject to a power to terminate, existing in the decedent as trustee in conjunction with two other trustees, nevertheless the Supreme Court held that section 302 (d) did not require the inclusion, in the gross estate of the decedent of the property subject to such power of termination. The Court held that the power to terminate existing in the decedent at the date of her death resulted from the action of the other trustees and not by virtue of any power reserved to herself as settlor in the original estate. The case, therefore, suggests that section 302 (d) may be circumvented in many ways so long as the power to alter, amend, revoke, or terminate does not accrue to the settlor by virtue of the reservation in the trust instrument.

It is, therefore, provided that section 302 (d) covers a power whether created at the time of transfer or thereafter arising from any source and whether exercisable in an individual or representative capacity. To some extent, it is believed this amendment is declaratory of existing law. To the extent that it is not so declaratory, it is prospective and will apply to transfers made after the date of enactment of the act. Section 206 also covers a power whether it exists jointly in the decedent and some other person or whether it exists only in some other person. This will apply to transfers made after the enactment of the act, since it is not declaratory of existing law. The Supreme Court in the case of *Helvering* v. *City Bank Farmers Trust Co.* (296 U. S. 85) has sustained the constitutionality of subjecting to the estate tax property which is subject to a power to be exercised by the decedent in conjunction with any person. Its conclusion was reached on the ground that the end sought to be attained was the prevention of tax avoidance by the device of qualifying the right to exercise the power so that it must be exercised in conjunction with another person who, however, would be selected by the decedent so as to comply with the decedent's wishes as to when and how the power should be exercised. If the person is selected to exercise the power with the decedent because he will comply with the decedent's wishes, it makes little difference whether the tax avoidance is effected by vesting in such person alone the sole right to exercise the power. In either case, such exercise will be governed by the wishes and directions of the decedent and will be sub-

ject to his control. It should, therefore, be embraced in section 302 (d).

Another change made in subsection (a) of section 206 has been to expressly include a power to terminate along with the powers to alter, amend, or revoke. In the case of *White* v. *Poor, supra,* the Supreme Court did not pass on the question of whether the power to terminate was included in the language relating to a power "to alter, amend or revoke." Since in substance a power to terminate is the equivalent of a power to revoke, this question should be set at rest. Express provision to that effect has been made and it is believed that it is declaratory of existing law.

* * * * *

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

No. 152

EVERIT B. TERHUNE, *et al.*, Executors under the will of WILLIAM L. TERHUNE,

Petitioners,

v.

WILLIAM M. WELCH, Collector.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF AS *AMICI CURIAE* AND BRIEF OF *AMICI CURIAE*

HUGH SATTERLEE,
WM. R. GREEN, JR.,
Amici Curiae,
30 Broad Street,
New York.

Pandick Press, Inc., 22 Thames St., New York, U. S. A.

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May it please the Court:

The undersigned respectfully move this Honorable Court for leave as *amici curiae* to file the accompanying brief in support of the petition for a writ of certiorari in this case.

HUGH SATTERLEE,
WM. R. GREEN, JR.,
Amici Curiae.

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BRIEF OF *AMICI CURIAE*

The Circuit Court of Appeals (126 Fed. (2d) 695), reversing the District Court (39 F. Supp. 430), has decided an important question of federal law which has not been, but should be, definitely settled by this Court, and has decided a federal question in a way probably in conflict with the principles of applicable decisions of this Court.

The decedent in 1929 transferred property to three trustees, of whom he was one, in trust for himself for life with remainder to his second wife and his children and their issue. As a result of her divorce from the decedent, the second wife's interest in the trust terminated before his death. The trust could be amended by consent of the surviving trustees and of the decedent's surviving children. He died on February 23, 1936. The Circuit Court held that

because of the power of amendment in the trustees and the principal beneficiaries the trust corpus was subject to inclusion in the gross estate for estate tax purposes under Section 302 (d) of the Revenue Act of 1926.

The Circuit Court reached its conclusion by construing Section 302 (d) as though it were in force as subsequently materially modified by the Revenue Act of 1936 at the time of the creation of the trusts and at the date of the decedent's death; by disregarding any difference between the capacity of the decedent as settlor and his relationship to the trust as trustee or beneficiary; by ignoring the limitations laid down in *Helvering* v. *City Bank Farmers Trust Co.* (296 U. S. 85) on the adoption by Congress of measures for the prevention of tax avoidance; by failing to consider the substantial similarity of the situation in *Helvering* v. *Helmholz* (296 U. S. 93); and by erroneously assuming that Congress had interpreted Section 302 (d) of the 1926 Act, before amendment in 1936, as covering a power exercisable by the decedent only as a trustee. The Circuit Court cited the decisions of this Court in *Helvering* v. *City Bank Farmers Trust Co.*, 296 U. S. 85; *Reinecke* v. *Smith*, 289 U. S. 172; and *White* v. *Poor*, 296 U. S. 98; and we believe misconstrued them, thereby confusing and confounding the construction of Section 302 (d) as in force prior to the 1936 Act and as still applicable to many trusts created prior to the 1936 Act.

In their petition and brief the attorneys for the petitioner have assigned and argued the important questions involved in their application. This brief will attempt to indicate additional reasons why these questions are entitled to consideration and decision by this Court.

Statute

Prior to 1924 the Revenue Acts of 1916 (Section 202(b)), 1918 (Section 402 (c)) and 1921 (Section 402 (c)) merely provided for inclusion in the gross estate of property with respect to which the decedent had made a transfer, or with respect to which he had created a trust, "intended to take effect in possession or enjoyment at or after his death".

The provision of the estate tax statute commonly known as Section 302 (d) was first enacted in the Revenue Act of 1924. It appeared in the Revenue Act of 1926 as follows:

> SEC. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated— . . .
>
> (d) To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, . . .

The only change from the 1924 Act was the substitution of the phrase, "by trust or otherwise," for the clause, "or with respect to which he has at any time created a trust." Section 302 was amended by the Joint Resolution of March 3, 1931, by Section 803 of the Revenue Act of 1932, and by Section 401 of the Revenue Act of 1934, but not as respects the above provision.

Section 805 of the Revenue Act of 1936 provided:

> SEC. 805. ESTATE TAXES—REVOCABLE TRANSFERS.
>
> (a) Section 302 (d) (1) of the Revenue Act of 1926, as amended, is amended to read as follows:

"(d) (1) To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona-fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, . . ."

(b) Except in the case of transfers made after the date of the enactment of this Act, no interest of the decedent of which he has made a transfer shall be included in the gross estate under such section 302 (d) (1) unless it was includible under such section before its amendment by this section.

Section 811 of the Internal Revenue Code, corresponding with old Section 302, provides:

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—. . .

(d) REVOCABLE TRANSFERS—

(1) TRANSFERS AFTER JUNE 22, 1936.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona-fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercis-

able) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, . . .

(2) TRANSFERS ON OR PRIOR TO JUNE 22, 1936.—To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, . . . Except in the case of transfers made after June 22, 1936, no interest of the decedent of which he has made a transfer shall be included in the gross estate under paragraph (1) unless it is includible under this paragraph; . . .

Argument

As appears above, there were three stages of the estate tax statute here pertinent, applicable respectively (1) to the period prior to enactment of the Revenue Act of 1924; (2) to the period between 1924 and the date of the enactment of the Revenue Act of 1936, June 22, 1936; and (3) to the period after June 22, 1936. In ascertaining the application of each statute the date of the transfer and not the date of death is determinative.

(1) As to trusts created prior to 1924, it is clear that the reservation of a power of amendment in the settlor conditioned upon consent of beneficiaries does not subject the trust corpus to inclusion in the gross estate.

In *Reinecke* v. *Northern Trust Company*, 278 U. S. 339, seven trusts had been created between 1903 and 1919 by the decedent, who died in 1922, by the terms of two of which a

power of revocation of the trusts was reserved to the settlor alone and by the terms of the remaining five of which a power to alter, change or modify the trust was reserved to the settlor with the concurrence of the single beneficiary or of a majority of the beneficiaries. The Court held that under Section 402 (c) of the Revenue Act of 1921 the first two trusts were subject to inclusion in the gross estate, but that the other five trusts had not been intended to take effect in possession or enjoyment at or after the decedent's death. As to the latter trusts, the Court said in part (p. 346):

> "Since the power to revoke or alter was dependent on the consent of the one entitled to the beneficial, and consequently adverse, interest, the trust, for all practical purposes, had passed as completely from any control by decedent which might inure to his own benefit as if the gift had been absolute.
>
> Nor did the reserved powers of management of the trusts save to decedent any control over the economic benefits or the enjoyment of the property. He would equally have reserved all these powers and others had he made himself the trustee, but the transfer would not for that reason have been incomplete."

(2) The effect of the 1924 amendment initiating the second stage of the statute was to subject to estate tax trusts in which the power of amendment existed in the decedent "in conjunction with any person". The scope of this extension was considered by the Court in 1935 for the first time in several cases.

In *Helvering* v. *City Bank Farmers Trust Company*, 296 U. S. 85, the question was whether or not Section 302 (d) of the Revenue Act of 1926 was applicable to a trust created in 1930, where the trust deed contained the reserva-

tion of a right in the settlor to modify, alter or revoke it with the written consent of the trustee, a trust company, and her husband, a beneficiary of the trust. The Court pointed out that the purpose of Congress in adding clause (d) by the 1924 Act "was to prevent avoidance of the tax by the device of joining with the grantor in the exercise of the power of revocation someone who he believed would comply with his wishes", and that "Congress may adopt a measure reasonably calculated to prevent avoidance of a tax"; but that "if the means are unnecessary or inappropriate to the proposed end, are unreasonably harsh or oppressive, when viewed in the light of the expected benefit, or arbitrarily ignore recognized rights to enjoy or to convey individual property, the guaranty of due process is infringed". The Court concluded:

> "In view of the evident purpose of Congress we find nothing unreasonable or arbitrary in the provisions of § 302 (d) of the Revenue Act of 1926 as applied in the circumstances of this case."

In *Helvering* v. *Helmholz,* 296 U. S. 93, consideration was given to the application of Section 302 (d) of the Revenue Act of 1926 in the case of a trust created in 1918 by a settlor, who was also a beneficiary, where the trust deed provided for termination of the trust, among other things, upon delivery to the trustee of a written instrument signed by all the then beneficiaries other than testamentary appointees declaring said trust term at an end. The Court held that, since under general law all parties in interest might terminate a trust, the questioned clause added nothing to the rights which existed without it, and further that, since the trust was created prior to the enactment of Section 302 (d), its retroactive operation would violate the Fifth Amendment.

In *White* v. *Poor,* 296 U. S. 98, the decedent, who died in 1931, created a trust, of which she was a life beneficiary, with herself and two other individuals as trustees, the trust deed providing that the trust might be terminated at any time by the person or persons who should then be trustees thereunder. "No power was reserved by Mrs. Sargent to modify the terms of the trust, and the recited power was never exercised." In 1920 Mrs. Sargent resigned as trustee and a successor was appointed by the remaining trustees to fill the vacancy, pursuant to the terms of the trust deed, and in 1921 the successor trustee resigned and the settlor was appointed to fill the vacancy. The Court remarked that the declaration of trust, technically speaking, contained no power to revoke, alter or amend the trust, what the instrument did being to make it possible for the trustees acting jointly to terminate the trust at any time, and that by her appointment as trustee in 1921 she acquired any power for the future solely by virtue of the action of the other trustees and the beneficiaries and "not in any sense by virtue of any power reserved to herself as settlor in the original declaration of trust". The Court concluded "that neither technically nor in substance does the power to terminate as it existed from 1921 to the date of Mrs. Sargent's death fall within Section 302 (d)".

Two other cases decided at the same time, involving the consequences of a possibility of reversion in the settlor, have since been overruled on that point by *Helvering* v. *Hallock,* 309 U. S. 106. In one of these, *Helvering* v. *St. Louis Union Trust Company,* 296 U. S. 39, the trust deed provided that the trustee had discretionary power to terminate the trust whenever the trustee might deem it wise to do so, but this provision was not regarded as material in either the majority or minority opinions of the Court. *Cf. Herzog* v. *Commissioner,* 116 Fed. (2d) 591, 595. In

the other, *Becker* v. *St. Louis Union Trust Company,* 296 U. S. 48, in the course of its discussion the Court made the following statement not affected by the subsequent reversal of its position on the main issue (p. 50):

> "By the declaration of trust here under review, the legal title, possession and control of the trust estate passed irrevocably from the grantor as an individual to himself as trustee. The effect is no different than if the trustee had been another person. Cf. Reinecke *v.* Northern Trust Co. 278 U. S. 339, 346."

(3) The ambiguity in the 1924 and 1926 Acts, to which the Court had adverted in *White* v. *Poor,* and the desire of Congress to secure additional revenue from the inclusion of gifts in trust in the gross estate, evidently impelled the Treasury Department to urge upon Congress amendments to Section 302 (d) broadening its scope. The Revenue Bill of 1936 (H. R. 12395) as introduced in the House of Representatives on April 21, 1936, and subsequently passed by the House, and as reported by the Senate Committee on Finance on June 1, 1936, contained no modification of Section 302 (d). As amended on the floor of the Senate and passed by the Senate on June 5, 1936, the bill contained a provision as follows:

> SEC. 807. ESTATE TAXES—REVOCABLE TRANSFERS.
>
> (a) Section 302 (d) (1) of the Revenue Act of 1926, as amended, is amended to read as follows:
>
> "(d) (1) To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona-fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through

> the exercise of a power (whether created at the time of such transfer or thereafter arising from any source, and whether exercisable in an individual or representative capacity) by the decedent alone or by the decedent in conjunction with any other person, to alter, amend, revoke, or terminate, . . ."
>
> (b) The amendment by subsection (a) of this section shall not apply to decedents dying prior to the date of the enactment of this Act.

In Conference Committee the House and Senate agreed on a modified provision, which was enacted as Section 805 of the Revenue Act of 1936, set forth above at page 5. (Conference Report, 74th Congress, 2d Session, Report No. 3068, page 19.)

A separate bill (H. R. 12793) to amend the internal revenue laws had been introduced in the House on May 20, 1936, but was not passed. Section 206 (a) of that bill proposed to amend Section 302 (d) along the lines of the original Senate amendment, but also subjecting to inclusion in the gross estate trusts in which someone exclusive of the settlor had the power of amendment. As to these abortive provisions, the Committee on Ways and Means in its report dated May 26, 1936 (74th Congress, 2d Session, Report No. 2818), at pages 9 and 10, commented as set forth in the appendix to the respondent's brief, at pages 11-13, and added:

> "The foregoing amendments to the estate tax laws are of great importance from a revenue standpoint. The total estate tax estimated for the present fiscal year will probably aggregate $200,000,000. Transfers will account for some $40,000,000 in taxes, against which it is estimated there will be credited gift taxes paid with respect to such transfers, of approximately $20,000,000. Transfers therefore account for net taxes of about $20,000,000. To the extent that such transfers may be made without subjecting the

> property transferred to the estate tax, the Government will lose a considerable amount of revenue. In view of the increased estate tax rates, it is probable also that taxpayers will be straining every effort to devise transfers which will permit them to retain control of their property during their lifetime and escape the imposition of estate taxes thereon. The proposed amendments are designed to plug up loop holes which now appear, so that taxpayers may not be successful in effecting tax avoidance."

This third stage of the statute was expressly made inapplicable to transfers prior to the date of the enactment of the 1936 Act, and the differentiation in the treatment of transfers before and of transfers after June 22, 1936, has been emphasized in Section 811 of the Code, set forth above at page 6. Whether or not in plugging up so-called loop holes as regards transfers after June 22, 1936, Congress has transcended the limits described in the opinion in the City Bank Farmers Trust Company case, *supra*, has apparently not yet been judicially decided.

At any rate, we are concerned with the proper construction of the statute, not in its first or third stage, but in its second stage, as it was in force between 1924 and 1936, a period of the creation of many trusts, in only a small proportion of which has the settlor since died. The estates of the settlors of such trusts, like the estate here, are entitled to the application of Section 302 (d) as originally enacted, without prejudice from the 1936 amendments.

Plainly the Circuit Court here was influenced by such amendments, relying on its understanding that Congress, as well as the Treasury, had interpreted the 1926 Act before amendment as covering a power in the decedent exercisable by him only as a trustee. This understanding is materially impaired by the consideration that the report of

the Ways and Means Committee, to which the Circuit Court refers, did not relate to the Revenue Bill of 1936, but to a separate bill which did not pass, and that the remark in the report to the effect that "to some extent it is believed this amendment is declaratory of existing law" does not specify which part of the amendment or at all amount to a statement of the intent of Congress in originally enacting Section 302 (d). Obviously this expression in the Committee's report was instigated by the Treasury Department, which in its regulations sought to make the 1936 statute retroactive in fact, although not in law. Prior to Regulations 80 (1937 edition) the regulations of the Treasury Department contain no such broad interpretation of Section 302 (d) in force prior to the 1936 amendments. See Regulations 70 (1929 edition), Article 19, and Regulations 80 (1934 edition), Article 20.

In the City Bank case (cited by the Circuit Court) the Court emphasized that the purpose of Congress in enacting Section 302 (d) was to prevent avoidance of the tax and that it could not arbitrarily ignore recognized rights to convey individual property. *Certainly the inclusion of a settlor as a trustee was a long recognized and normal concomitant of the creation of a trust, without any thought of tax avoidance, and in the present case no inference of a purpose of tax avoidance may be drawn from the record.* The long recognized distinction between a person in his individual capacity and in the capacity of trustee required more than the inexpressive language of the original 1926 Act to obliterate it. (*Cf. Becker* v. *St. Louis Union Trust Company, supra,* page 11.) In the Helmholz case the settlor was a beneficiary, and if the 1936 amendments be imputed to Section 302 (d) as it existed before them, then the statute was even more applicable to a beneficiary than to a trustee. It is noteworthy that the power was in the "then" bene-

ficiaries, excluding successor beneficiaries by appointment or otherwise under the terms of the trust. In the Poor case (cited by the Circuit Court), again disregarding the limited scope of the statute in the absence of the 1936 amendments and giving the language an unreasoning literal effect, the decedent at the date of her death did share in a power of amendment, although it existed in her fortuitously as a trustee and not in herself as settlor.

The Circuit Court also relied on *Reinecke* v. *Smith*, 289 U. S. 172, an income tax case under a different statute, which turned on whether or not a trustee as such was a beneficiary of the trust. The trust deed provided that the trust might be "modified or revoked at any time by an instrument in writing signed by Douglas Smith (the grantor) and either one of the other two trustees or their successors". This Court held that a trustee as such was not a beneficiary, saying in part:

> "Both words have a common and accepted meaning; the former signifies the person who holds title to the *res* and administers it for the benefit of others; the latter the *cestui que trust* who enjoys the advantages of such administration."

There the settlor as such, and not as a trustee or beneficiary, had the power specified by the statute. Whether or not he was a trustee had no significance.

We believe that enough has been said to show that serious and important questions of estate tax law are involved in the Terhune case. Rightly or wrongly the decision of the Circuit Court of Appeals came as a shock to lawyers concerned with trusts and estates. There are undoubtedly a great number of trusts created before 1936, which the trustees are empowered to modify or terminate. In many of these the settlor is one of the trustees or entitled to appoint

trustees. Each such situation, as the result of the Circuit Court's decision, presents a potential controversy as to whether or not Section 302 (d) is applicable. Regardless of the soundness of the decision of the Circuit Court, it will materially further the orderly administration of justice if the Court will in this case clarify the application and construction of Section 302 (d), which in its form before the 1936 amendments is still very much a live statute (I. R. C., Section 811, *supra*, page 6).

Conclusion

It is at least doubtful that to Section 302 (d) of the 1926 Act before amendment should be ascribed the enlarged meaning of the express language of the 1936 Act. That doubt must be resolved in favor of the taxpayer. *Cf. Reinecke* v. *Northern Trust Co.*, 278 U. S. 339, 348. It is respectfully submitted that the petition for a writ of certiorari herein should be granted.

HUGH SATTERLEE,
WM. R. GREEN, JR.,
Amici Curiae.